

**REPORT OF THE AUDIT OF THE
FORMER ADAIR COUNTY
SHERIFF'S SETTLEMENT - 2006 TAXES**

**For The Period
April 29, 2006 Through December 31, 2006**



**CRIT LUALLEN
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EXECUTIVE SUMMARY

**AUDIT EXAMINATION OF THE
FORMER ADAIR COUNTY
SHERIFF'S SETTLEMENT - 2006 TAXES**

**For The Period
April 29, 2006 Through December 31, 2006**

The Auditor of Public Accounts has completed the audit of the Sheriff's Settlement - 2006 Taxes for former Adair County Sheriff for the period April 29, 2006 through December 31, 2006. We have issued an unqualified opinion on the financial statement taken as a whole. Based upon the audit work performed, the financial statement is presented fairly in all material respects.

Financial Condition:

The former Sheriff collected taxes of \$3,305,869 for the districts for 2006 taxes, retaining commissions of \$136,399 to operate the Sheriff's office. The former Sheriff distributed taxes of \$3,165,144 to the districts for 2006 Taxes.

Report Comment:

- The Former Sheriff's Office Lacked Adequate Segregation Of Duties

Deposits:

The former Sheriff's deposits as of November 8, 2006 were exposed to custodial credit risk as follows:

- Uncollateralized and Uninsured \$269,428

The former Sheriff's deposits were covered by FDIC insurance and a properly executed collateral security agreement, but the bank did not adequately collateralize the former Sheriff's deposits in accordance with the security agreement.

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CRIT LUALLEN
AUDITOR OF PUBLIC ACCOUNTS

To the People of Kentucky

Honorable Steven L. Beshear, Governor

Jonathan Miller, Secretary

Finance and Administration Cabinet

Honorable Ann Melton, Adair County Judge/Executive

Honorable Steve Cheatham, Former Adair County Sheriff

Honorable Ralph Curry, Adair County Sheriff

Members of the Adair County Fiscal Court

Independent Auditor's Report

We have audited the former Adair County Sheriff's Settlement - 2006 Taxes for the period April 29, 2006 through December 31, 2006. This tax settlement is the responsibility of the former Adair County Sheriff. Our responsibility is to express an opinion on this financial statement based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America, the standards applicable to financial audits contained in Government Auditing Standards issued by the Comptroller General of the United States, and the Audit Guide for Sheriff's Tax Settlements issued by the Auditor of Public Accounts, Commonwealth of Kentucky. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statement is free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statement. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

As described in Note 1, the Sheriff's office prepares the financial statement on a prescribed basis of accounting that demonstrates compliance with the modified cash basis, which is a comprehensive basis of accounting other than accounting principles generally accepted in the United States of America.

In our opinion, the accompanying financial statement referred to above presents fairly, in all material respects, the former Adair County Sheriff's taxes charged, credited, and paid for the period April 29, 2006 through December 31, 2006, in conformity with the modified cash basis of accounting.

In accordance with Government Auditing Standards, we have also issued our report dated January 18, 2008 on our consideration of the Sheriff's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with Government Auditing Standards and should be considered in assessing the results of our audit.



To the People of Kentucky

Honorable Steven L. Beshear, Governor

Jonathan Miller, Secretary

Finance and Administration Cabinet

Honorable Ann Melton, Adair County Judge/Executive

Honorable Steve Cheatham, Former Adair County Sheriff

Honorable Ralph Curry, Adair County Sheriff

Members of the Adair County Fiscal Court

Based on the results of our audit, we present the accompanying comment and recommendation, included herein, which discusses the following report comment:

- The Former Sheriff's Office Lacked Adequate Segregation Of Duties

Respectfully submitted,

A handwritten signature in black ink, appearing to read "Crit Luallen", written in a cursive style.

Crit Luallen

Auditor of Public Accounts

January 18, 2008

ADAIR COUNTY
STEVE CHEATHAM, FORMER SHERIFF
SHERIFF'S SETTLEMENT - 2006 TAXES

For The Period
April 29, 2006 Through December 31, 2006

<u>Charges</u>	<u>County Taxes</u>	<u>Special Taxing Districts</u>	<u>School Taxes</u>	<u>State Taxes</u>
Real Estate	\$ 392,640	\$ 608,813	\$ 1,782,321	\$ 564,696
Tangible Personal Property	41,682	47,535	111,603	96,348
Fire Protection	2,232			
Increases Through Exonerations	15	23	69	179
Franchise Taxes	29,218	34,299	85,721	
Additional Billings	12	18	53	17
Bank Franchises	48,092			
Adjusted to Sheriff's Receipt	167	878	1,974	280
Gross Chargeable to Sheriff	514,058	691,566	1,981,741	661,520
<u>Credits</u>				
Exonerations	2,653	3,761	10,519	3,588
Discounts	6,658	8,530	24,526	8,580
Franchise Taxes	2	2	6	
Transferred to Incoming Sheriff	56,250	86,180	251,266	80,495
Total Credits	65,563	98,473	286,317	92,663
Taxes Collected	448,495	593,093	1,695,424	568,857
Less: Commissions *	19,349	24,769	67,817	24,464
Taxes Due	429,146	568,324	1,627,607	544,393
Taxes Paid	428,651	567,535	1,625,315	543,643
Refunds (Current and Prior Year)	495	789	2,292	750
Due Districts as of Completion of Audit	\$ 0	\$ 0	\$ 0	\$ 0

* Commissions:

10% on \$	10,000
4.25% on \$	1,425,683
4% on \$	1,870,186

The accompanying notes are an integral part of this financial statement.

ADAIR COUNTY
NOTES TO FINANCIAL STATEMENT

December 31, 2006

Note 1. Summary of Significant Accounting Policies

A. Fund Accounting

The Sheriff's office tax collection duties are limited to acting as an agent for assessed property owners and taxing districts. A fund is used to account for the collection and distribution of taxes. A fund is a separate accounting entity with a self-balancing set of accounts. Fund accounting is designed to demonstrate legal compliance and to aid financial management by segregating transactions related to certain government functions or activities.

B. Basis of Accounting

The financial statement has been prepared on a modified cash basis of accounting. Basis of accounting refers to when charges, credits, and taxes paid are reported in the settlement statement. It relates to the timing of measurements regardless of the measurement focus.

Charges are sources of revenue which are recognized in the tax period in which they become available and measurable. Credits are reductions of revenue which are recognized when there is proper authorization. Taxes paid are uses of revenue which are recognized when distributions are made to the taxing districts and others.

C. Cash and Investments

At the direction of the fiscal court, KRS 66.480 authorizes the Sheriff's office to invest in the following, including but not limited to, obligations of the United States and of its agencies and instrumentalities, obligations and contracts for future delivery or purchase of obligations backed by the full faith and credit of the United States, obligations of any corporation of the United States government, bonds or certificates of indebtedness of this state, and certificates of deposit issued by or other interest-bearing accounts of any bank or savings and loan institution which are insured by the Federal Deposit Insurance Corporation (FDIC) or which are collateralized, to the extent uninsured, by any obligation permitted by KRS 41.240(4).

Note 2. Deposits

The former Sheriff maintained deposits of public funds with depository institutions insured by the Federal Deposit Insurance Corporation (FDIC) as required by KRS 66.480(1)(d). According to KRS 41.240(4), the depository institution should pledge or provide sufficient collateral which, together with FDIC insurance, equals or exceeds the amount of public funds on deposit at all times. In order to be valid against the FDIC in the event of failure or insolvency of the depository institution, this pledge or provision of collateral should be evidenced by an agreement between the Sheriff and the depository institution, signed by both parties, that is (a) in writing, (b) approved by the board of directors of the depository institution or its loan committee, which approval must be reflected in the minutes of the board or committee, and (c) an official record of the depository institution.

ADAIR COUNTY
NOTES TO FINANCIAL STATEMENT
December 31, 2006
(Continued)

Note 2. Deposits (Continued)

Custodial Credit Risk - Deposits

Custodial credit risk is the risk that in the event of a depository institution failure, the Sheriff's deposits may not be returned. The former Sheriff did not have a deposit policy for custodial credit risk but rather followed the requirements of KRS 41.240(4). As of December 31, 2006, all deposits were covered by FDIC insurance or a properly executed collateral security agreement. However, as of November 8, 2006, public funds were exposed to custodial credit risk because the bank did not adequately collateralize the former Sheriff's deposits in accordance with the security agreement as follows:

- Uncollateralized and Uninsured \$269,428

Note 3. Tax Collection Period

The real and personal property tax assessments were levied as of January 1, 2006. Property taxes were billed to finance governmental services for the year ended June 30, 2007. Liens are effective when the tax bills become delinquent. The collection period for these assessments was September 21, 2006 through December 31, 2006.

Note 4. Interest Income

The former Adair County Sheriff earned \$2,747 as interest income on 2006 taxes. The former Sheriff distributed the appropriate amount to the school district as required by statute, and the remainder was used to operate the Sheriff's office.

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REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON
COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF THE FINANCIAL
STATEMENT PERFORMED IN ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS



CRIT LUALLEN
AUDITOR OF PUBLIC ACCOUNTS

The Honorable Ann Melton, Adair County Judge/Executive
Honorable Steve Cheatham, Former Adair County Sheriff
Honorable Ralph Curry, Adair County Sheriff
Members of the Adair County Fiscal Court

Report On Internal Control Over Financial Reporting And On
Compliance And Other Matters Based On An Audit Of The Financial
Statement Performed In Accordance With Government Auditing Standards

We have audited the former Adair County Sheriff's Settlement - 2006 Taxes for the period April 29, 2006 Through December 31, 2006, and have issued our report thereon dated January 18, 2008. The Sheriff prepares his financial statement in accordance with a basis of accounting other than generally accepted accounting principles. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in Government Auditing Standards issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the former Adair County Sheriff's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the former Adair County Sheriff's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the former Adair County Sheriff's internal control over financial reporting.

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and would not necessarily identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses. However as discussed below, we identified a certain deficiency in internal control over financial reporting that we consider to be a significant deficiency.

A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the entity's ability to initiate, authorize, record, process, or report financial data reliably in accordance with the modified cash basis of accounting which is a basis of accounting other than generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the entity's financial statement that is more than inconsequential will not be prevented or detected by the entity's internal control over financial reporting. We consider the deficiency described in the accompanying comment and recommendation to be a significant deficiency in internal control over financial reporting.

- The Former Sheriff's Office Lacked An Adequate Segregation Of Duties



Report On Internal Control Over Financial Reporting And
On Compliance And Other Matters Based On An Audit Of The Financial
Statement Performed In Accordance With Government Auditing Standards
(Continued)

Internal Control Over Financial Reporting (Continued)

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statement will not be prevented or detected by the entity's internal control. Our consideration of the internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in the internal control that might be significant deficiencies and, accordingly, would not necessarily disclose all significant deficiencies that are also considered to be material weaknesses. However, we consider the significant deficiency described above to be a material weakness.

Compliance And Other Matters

As part of obtaining reasonable assurance about whether the former Adair County Sheriff's Settlement – 2006 Taxes for the period April 29, 2006 through December 31, 2006 is free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under Government Auditing Standards.

This report is intended solely for the information and use of management, the Adair County Fiscal Court, and the Kentucky Governor's Office for Local Development and is not intended to be and should not be used by anyone other than these specified parties.

Respectfully submitted,



Crit Luallen
Auditor of Public Accounts

January 18, 2008

COMMENT AND RECOMMENDATION

ADAIR COUNTY
STEVE CHEATHAM, FORMER SHERIFF
COMMENT AND RECOMMENDATION

For The Period
April 29, 2006 Through December 31, 2006

INTERNAL CONTROL - SIGNIFICANT DEFICIENCY AND MATERIAL WEAKNESS:

The Former Sheriff's Office Lacked Adequate Segregation Of Duties

The former Sheriff's office lacked segregation of duties over receipts and disbursements. The former Sheriff's bookkeeper collected payments from customers, opened mail, prepared deposits, prepared checks, and reconciled the bank account. In the bookkeepers absence another employee performed these duties. The former Sheriff did not document oversight of these activities. The former Sheriff should have segregated duties or implemented the following compensating controls to offset this internal control weakness:

- The former Sheriff should have compared daily bank deposits with daily collection reports. This could have been documented by initialing the daily report and bank deposit.
- The former Sheriff should have compared monthly tax reports to the receipts and disbursements ledgers. Any differences should have been reconciled. This could have been documented by initialing the monthly tax reports, receipts ledger, and disbursements ledger.
- The former Sheriff should have frequently recounted and deposited daily cash receipts. This could have been documented by initialing bank deposit slips.
- The former Sheriff should have examined tax distribution checks prepared by another employee and agreed tax distributions to monthly tax reports. This could have been documented by signing monthly tax reports and checks.
- The former Sheriff should have delivered tax distribution checks and a copy of monthly tax reports to taxing districts. The former Sheriff should have received a signed receipt documenting delivery.
- The former Sheriff should have reviewed monthly bank reconciliations prepared by another employee and compared the reconciliation to the checkbook balance. Any differences should have been reconciled. The former Sheriff could have documented this by initialing the bank reconciliation and the balance in the checkbook.

Former Sheriff's Response: No response provided.

